

UNITED STATES OF AMERICA
FEDERAL ENERGY REGULATORY COMMISSION

Before Commissioners: Joseph T. Kelliher, Chairman;
Nora Mead Brownell, and Suedeene G. Kelly.

ExTex LaPorte Limited Partnership

Docket No. EG06-36-000

ORDER DENYING APPLICATION FOR DETERMINATION
OF EXEMPT WHOLESALE GENERATOR STATUS

(Issued May 30, 2006)

1. On February 7, 2006, as amended on March 31, 2006, ExTex LaPorte Limited Partnership (ExTex) filed an application for determination of exempt wholesale generator (EWG) status pursuant to section 32 of the Public Utility Holding Company Act of 1935, as amended by the Energy Policy Act of 1992 (PUHCA 1935).¹ In this order, we deny the Applicant's request for EWG status based on the discussion below.

I. Background

2. ExTex owns and operates three electric generating facilities, each located in Texas, and sells the output of them exclusively at wholesale within the Electric Reliability Council of Texas (ERCOT) market. ExTex's generating facilities are ExTex LaPorte Generating Station, a 165 MW combustion turbine generating facility located in LaPorte, Texas; Handley Generating Station (Handley), a 1,440 MW gas-fired steam turbine generating facility located in Fort Worth, Texas; and Mountain Creek Generating Station (Mountain Creek), a 894 MW gas-fired steam turbine generating facility located near Dallas, Texas.

¹ 15 U.S.C. § 79z-5a (2000), *repealed by* the Energy Policy Act of 2005, Pub. L. No. 109-58, §1263, 119 Stat. 594, 974 (2005). As the application was filed prior to the date the repeal of PUHCA 1935 was to take effect, review of this application is governed by the requirements of PUHCA 1935.

3. In its prior orders granting EWG status to ExTex, the Commission has recognized that each of ExTex's generating facilities is an "eligible facility," as that term is defined in PUHCA 1935 section 32.

4. Applicant submitted a sworn statement by a representative legally authorized to bind Applicant stating that:

a) ExTex is and will be engaged directly, or indirectly through one or more affiliates as defined in section 2(a)(11)(B) of PUHCA 1935, and exclusively in the business of owning or operating, or both owning and operating, all or part of one or more eligible facilities, and selling electric energy exclusively at wholesale, provided that the Commission determines that ExTex's lease of mineral rights at Handley will not violate the EWG exclusivity requirement.

b) ExTex is not currently engaged in sales of power at retail.

c) The circumstances described in section 365.3(a)(1)(iii) of the Commission's regulations will not apply to ExTex, since ExTex will satisfy the "and selling electric energy at wholesale" requirement as both an owner and operator of eligible facilities and as the person selling electric energy at wholesale from eligible facilities.

d) All the eligible facilities under ExTex's ownership and control are and will continue to be interconnected with the ERCOT transmission system. ExTex does not and will not own or operate transmission facilities other than step-up transformers and generator lead lines necessary to interconnect the eligible facilities with the ERCOT transmission system, as well as various other types of equipment and facilities typically associated with a generating plant, such as spare parts, control equipment, and site fencing and drainage systems.

e) Other than as described in its application, there are no lease arrangements through which ExTex will lease the eligible facilities to a public utility company or any other party.

f) ExTex is a limited partnership, comprised of a general partner, Exelon General, and a limited partner, Exelon Limited. Exelon General and Exelon Limited are limited liability companies headquartered in Pennsylvania.

g) No rate or charge for, or in connection with, the construction of the ExTex facility, or for electric energy produced by the ExTex facility (other than any portion of a rate or charge which represents recovery of the cost of a wholesale rate or charge) was in effect under the laws of any state on October 24, 1992. Rates and charges reflecting the

costs of the Handley and Mountain Creek Facilities were in effect in Texas on October 24, 1992. On June 5, 2001, the Public Utilities Commission of Texas (PUCT) issued an order determining that allowing generation facilities currently in TXU Electric's rate base, which include the Handley and Mountain Creek Facilities, to be "eligible facilities" as defined in PUHCA 1935: (1) will benefit consumers, (2) is in the public interest, and (3) does not violate Texas law. ExTex provided a copy of the PUCT order in its application for EWG status in Docket No. EG02-60-000 filed December 21, 2001, as amended January 9, 2002.

h) ExTex is associated with the following electric utility companies, as defined in section 2(a)(3) of PUHCA 1935: PECO Energy; Commonwealth Edison; and Exelon Generation.

i) No portion of the eligible facilities owned by ExTex will be owned or operated by an electric utility company that is an affiliate or associate company of ExTex.

j) ExTex will or may engage in certain activities incidental to the sale of electric energy at wholesale as previously authorized by the Commission. These activities include: (a) wholesale marketing and brokering of electric energy that ExTex facilities have not generated; (b) selling excess gas supplies and reassigning excess transmission capacity originally obtained to effect a specific wholesale sale of electric energy; (c) entering into contracts for transmission capacity solely to the extent necessary to effect sales at wholesale of electricity generated by ExTex facilities or others; (d) trading emission allowances associated with the normal operations of the Facilities; (e) and electric generation development activities.

5. ExTex states that Handley is located on an approximately 270-acre site situated in the vicinity of the Barnett Shale gas field north of Fort Worth, Texas. ExTex asserts that it owns the mineral rights underlying Handley. ExTex explains that it has the opportunity to lease these mineral rights to an unaffiliated gas and oil² exploration and production company to attempt to realize the potential value of the natural gas underlying the property.

² ExTex expects that drilling would be unlikely to produce economic quantities of oil. Accordingly, ExTex expects that it will not earn any revenues from oil production.

6. ExTex requests a determination by the Commission that its lease of mineral rights for natural gas exploration and production will be incidental to ExTex's business of being "engaged... exclusively in the business of owning or operating, or both owning and operating, all or part of one or more eligible facilities and selling electric energy at wholesale," such that ExTex may maintain its status as an EWG with such a mineral rights lease in place.

7. According to ExTex, the lease is expected to be a three-year mineral rights lease with an unaffiliated gas and oil exploration and production company with terms and conditions consistent with industry-standard lease provisions. Under such a standard-term lease, ExTex expects that it would earn royalties for gas and oil produced at the Handley site approximately equal to twenty-five percent of the market value of such production, together with a one-time lease bonus payment. ExTex expects that the value of the mineral rights underlying Handley over the projected ten to twenty year life of a mineral rights lease, together with the value of drilling bonuses, could be up to \$6.3 million on a net present value basis.

8. ExTex expects that it could arrange the terms of the lease to have the lessee pay all royalties and lease bonuses to ExTex in the form of either cash or in natural gas that ExTex could use in the electric generating process at any of its three gas-fired generating facilities. If ExTex arranges for payment in natural gas in-kind, the amount of gas it would be paid over the term of the lease would be a fraction of the total amount of gas it will consume in the power generation process over that period. During that period, if ExTex's mineral rights lessee makes payments of natural gas in-kind at times when ExTex does not need the gas (because of outages or dispatch decisions), ExTex would store the gas using gas storage arrangements it already has in place to manage its existing gas supplies. ExTex states that, similarly, if its mineral rights lessee paid royalties in cash, the revenues ExTex would be paid under the lease would be a fraction of the expense for the natural gas ExTex would purchase for power generation purposes during the lease term.

9. ExTex contends that its entitlement to the natural gas produced from the wells at Handley or the cash equivalent, would be equal to approximately 25 percent of the wells' output. Accordingly, the lease would supply only a small fraction of the natural gas ExTex will consume for fuel production during the lease term. At the royalty rate of approximately 25 percent, the natural gas wells at Handley would be expected to supply ExTex with only approximately 1.5 percent of its annual fuel requirement during the first year of gas production, a figure that would decline to approximately 0.125 percent during the later years of the lease. Over the term of the lease, the wells would be expected to supply approximately 0.375 percent of ExTex's fuel requirements during that period.

10. ExTex argues that the instant situation is analogous to that in *PSEG Fossil, LLC*, 95 FERC ¶ 61,405 (2001) (*PSEG Fossil*), in which the Commission permitted owners of generating stations to lease land to a synthetic fuel manufacturer that would produce and supply fuel for use in the production of electricity at those stations. We concluded, “[s]ince a fuel supply is essential to Applicants’ business as generators of electric energy at wholesale, and the SynFuel operations are sized no larger than the amount of fuel applicants expect to need, the receipt of lease payments as the result of an activity to obtain that fuel supply does not violate the exclusivity requirement.”³

11. ExTex contends that, similar to the situation in *PSEG Fossil*, the natural gas wells proposed to be drilled will produce no more fuel than ExTex will need to fuel its natural gas-fired generating facilities during the term of the lease. ExTex reiterates that the wells would produce only approximately 1.5 percent of ExTex’s total fuel requirements during the lease period, and the mineral rights lease could supply ExTex with only approximately 0.375 percent of its fuel requirements during that period.

12. ExTex asserts that natural gas is an essential input to ExTex’s business of exclusively owning and operating eligible facilities - two of which are fueled with natural gas - and selling electric energy at wholesale, just as the supply of synthetic fuel was essential to the *PSEG Fossil* applicants’ business of exclusively generating power and selling it at wholesale.

13. ExTex asserts that its lease of mineral rights at Handley for payment of natural gas in-kind for use in ExTex’s wholesale electric generating activities will be wholly consistent with *PSEG Fossil* and does not violate the exclusivity requirement for EWG status. ExTex believes that its lessee’s payment of mineral rights lease royalties to ExTex in cash also would be consistent with *PSEG Fossil* and would not cause ExTex to violate the exclusivity requirement. In *PSEG Fossil*, the lessee paid rent to the EWG lessors in cash and supplied synthetic fuel to the lessors pursuant to a fuel procurement contract. ExTex contends that *PSEG Fossil* provides a precedent for allowing ExTex’s mineral rights lessee to pay cash royalties to ExTex. ExTex claims that the substance of a cash payment would be the same to ExTex as a payment of natural gas in-kind: both forms of payment would support and be essential to ExTex’s exclusive wholesale power generation business, the cash payment allowing ExTex to procure natural gas for power generation fuel, the natural gas in-kind constituting a direct provision of fuel. ExTex

³ *PSEG Fossil*, 95 FERC at 62,505.

requests that the Commission determine that its lease of mineral rights at Handley will not violate the EWG exclusivity requirement regardless of the form - cash or natural gas - in which ExTex would be paid under that lease.

14. ExTex contends that the parallels between the facts in its application and in *PSEG Fossil* extend to the ability of the lessee in both cases to sell its product not supplied to the lessor. According to ExTex, in *PSEG Fossil*, the applicants' contracts with their synthetic fuel manufacturer lessee provided that the applicants would purchase the entire output of the lessee's synthetic fuel facilities, but that they would be relieved of their purchase obligations under certain circumstances, including changes in generation dispatch rates that reduced the applicants' need for fuel. ExTex states that the synfuel manufacturer was free to sell to third parties any fuel not purchased by the applicants. ExTex claims that, similarly, ExTex's lessee would be free to sell the natural gas produced at its wells but not supplied to ExTex.

15. ExTex also contends that its proposed mineral rights lease is consistent with Congress' and the Commission's policies with respect to EWGs in another way. According to ExTex, the Commission allows EWGs, including ExTex, to resell gas supplies and transportation capacity in excess of that needed for their facilities when the facilities are not operating at full capacity.⁴ ExTex claims that, in allowing such incidental transactions, the Commission noted Congress's apparent intent that such transactions be considered incidental so as to not require entities to waste resources associated with their exclusive EWG-related activities. ExTex asserts that, as Handley happens to be situated atop a potentially valuable natural gas field, it would be wasteful to deprive ExTex of the opportunity to tap the natural gas resources underlying Handley.

II. Notice of Filing

16. Notice of the application and amendment were published in the *Federal Register*, 71 Fed. Reg. 8575 (2006), with comments, interventions, and protests due on or before May 24, 2006. None was filed.

⁴ ExTex Amendment at 5, citing *Selkirk Cogen Partners, LP*, 69 FERC ¶ 61,037 (1994) (*Selkirk Cogen*).

III. Discussion

17. Based on the information in the application and amendment thereto, and for the reasons discussed below, we find that ExTex is not an EWG as defined in section 32(a)(1) of PUHCA 1935, and therefore deny its application.

18. Section 32(a) of PUHCA 1935 and implementing regulations of the Commission provide that EWGs must be engaged *exclusively* in the business of owning and/or operating eligible facilities and selling electric energy at wholesale. While we found that the applicants in *PSEG Fossil* did not violate the exclusivity requirements by their leasing activities, we find that the situation in *PSEG Fossil* is distinguishable from the instant facts.

19. First, *PSEG Fossil* is distinguishable from the present case in that the applicants in *PSEG Fossil* were required to purchase the entire output of the synthetic fuel facilities (while there is no such requirement in ExTex's leasing proposal). ExTex states that the "synfuel manufacturer [in *PSEG Fossil*] was free to sell to third parties any fuel not purchased by the applicants" and that "[s]imilarly, ExTex LaPorte's lessee would be free to sell the natural gas produced at its wells but not supplied to ExTex LaPorte."⁵ However, ExTex fails to point out that the synfuel manufacturer in *PSEG Fossil* would be limited in its opportunities to sell to third parties (for example, only when the applicants would not be able to purchase fuel because of, *e.g.*, force majeure or outages).

20. Additionally, the lease in *PSEG Fossil* was tied to the construction and operation of "synthetic fuel manufacturing facilities that are essential to Applicants' fuel supply. Since a fuel supply is essential to Applicants' business as generators of electric energy at wholesale, and the SynFuel operations are sized no larger than the amount of fuel applicants expect to need, the receipt of lease payments as the result of an activity to obtain that fuel supply does not violate the exclusivity requirement."⁶ ExTex focuses on how, in *PSEG Fossil*, the operations of the property at issue were "sized no larger than the amount of fuel applicants expect to need" and that "[s]imilarly, the natural gas wells proposed to be drilled by . . . [l]essee will produce no more fuel than ExTex LaPorte will need to fuel its natural gas-fired generating facilities during the term of the lease."⁷

⁵ ExTex Amendment at 4.

⁶ *PSEG Fossil*, 95 FERC at 62,506.

⁷ ExTex Amendment at 4.

However, the contractual intent here is that 75 percent or more of the natural gas produced would be sold for use by entities other than ExTex, while none or little of the fuel in *PSEG Fossil* was expected to be sold for use by others.

21. The instant facts are also distinguishable from the situation in *Selkirk Cogen*, which ExTex also relies on. As mentioned previously, ExTex states that its

proposed mineral rights lease is consistent with Congress's and FERC's policy with respect to EWGs in another way. FERC allows EWGs, including ExTex LaPorte, to resell gas supplies and transportation capacity in excess of that needed for their facilities when the facilities are not operating at full capacity.^[8]

22. However, the gas that would be sold by the lessees in the instant case would not be that resulting from the facility "not operating at full load because of either dispatch or availability constraints, or as a result of ambient conditions . . ."⁹ The gas to be sold by ExTex's lessees is that resulting from activities that are separate from electric generation. ExTex goes on to state that "[i]n allowing such incidental transactions, FERC noted Congress's apparent intent that such transactions be considered incidental so as to not require entities to waste resources associated with their exclusive EWG-related activities."¹⁰ In the present case, leasing mineral rights underlying Handley has little connection, if any, with ExTex's electric generating activities, outside the fact that the Handley station "happens to be situated atop a potentially valuable natural gas field."¹¹

23. Accordingly, we deny ExTex's arguments that its situation falls within the bounds of our prior determinations in *PSEG Fossil* and *Selkirk Cogen*, and therefore deny its application for EWG status because its proposed leasing activities do not meet the exclusivity requirement (*i.e.*, that applicants solely own and/or operate part or all of an eligible facility or eligible facilities while making wholesale electric energy sales). ExTex's proposed leasing activities, as described in its application, are not activities incidental to the sale of electric energy at wholesale.

⁸ *Id.* at 5.

⁹ *Selkirk Cogen*, 69 FERC at 61,167.

¹⁰ ExTex Amendment at 5.

¹¹ *Id.*

24. This result does not mean that the natural gas here must go undeveloped. ExTex can transfer its mineral rights to another entity, even an affiliate, and also may receive a fixed payment for these rights. Having ExTex transfer the asset in this way is distinguishable from the ongoing stake it would have in the natural gas business under its proposed arrangement. The transferee then may lease the rights to a developer, and receive a share of the natural gas (or cash equivalent) produced over time from the rights. This approach will allow development of the resource, and still honor the restriction imposed by Congress that EWGs must engage exclusively in the business of selling wholesale power, not in other businesses.

The Commission orders:

Accordingly, based on the information contained in this application, the Commission denies ExTex's application for EWG status as defined in section 32(a)(1) of PUHCA 1935.

By the Commission.

(S E A L)

Magalie R. Salas,
Secretary.